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E.O. 12958: DECL: 02/07/2017  
TAGS: [ENRG](#) [EINV](#) [ECON](#) [PREL](#) [EC](#)  
SUBJECT: AMBASSADOR'S MEETING WITH MINISTER OF ENERGY ACOSTA  
REF: A. QUITO 173

[1](#)B. 06 QUITO 2807  
[1](#)C. 06 QUITO 1735

Classified By: AMBASSADOR LINDA JEWELL. REASON: 1.4 B AND D

[1](#)1. (C) Summary. In a wide-ranging meeting with the Ambassador, Minister of Energy Acosta presented himself as a problem-solver. He said that he intends to solve the problems of U.S.-owned electric generator Machala Power and would study the situation of City Oriente, a small U.S.-owned petroleum company. He wants to bring more low-cost electricity generators on-line, find a solution to the long-festering problems for Guayaquil's electricity company, and promote the production and use of natural gas. Acosta criticized the GOE's existing oil production contracts with private oil companies and said that bilateral investment treaties are not the solution to Ecuador's investment woes. However, he was silent on what, if anything, the GOE will do about falling oil production. End summary.

[1](#)2. (C) The Ambassador met with Minister of Energy and Mines Alberto Acosta on February 2. Acosta opened the meeting by stressing the importance for Ecuador of maintaining good relations with the United States. He said that this may not always be easy, but we should maintain relations based on mutual respect, and that he would always have an open door for the Ambassador. The Ambassador responded that the United States has commercial disagreements with our largest trading partners, such as Canada, and that it is critical to address these disagreements in their proper channels and not allow them to affect the broader relationship.

U.S. Energy Companies  
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[1](#)3. (C) Acosta said that the government's relations with U.S. companies are "complex" and he intends to resolve them "bit by bit." The Ambassador said that resolving problems with U.S. companies would allow them to increase their investment in Ecuador and help address Ecuador's energy needs. She noted Machala Power's interest in doubling its generating capacity.

[1](#)4. (C) Acosta made the following comments on U.S. energy companies:

Machala Power: He met with Machala Power, understands its problem, and intends to find a solution since Machala Power is prepared to boost Ecuador's generating capacity. He said a complicating factor is that Machala Power has filed for arbitration, to which the Ambassador replied that Machala

Power would prefer a negotiated solution. (Note: the GOE has failed to compensate Machala Power for insufficient payments by electricity distributors.)

City Oriente: He opened with a broad statement that the current oil production contracts are unfavorable for Ecuador.

The Ambassador noted that City Oriente is a small company which is relying heavily on loans, which limits its flexibility. Acosta replied that he would study the matter, but cautioned that any special treatment for City Oriente would be carefully scrutinized by the other oil companies. (Note: The revised hydrocarbons law requires City Oriente to share 50% of extraordinary revenue with the GOE, which City Oriente maintains it cannot do and service its debt. The outgoing administration failed to develop a solution to City's dilemma.)

Occidental Petroleum: Acosta said that the Oxy case is "complicated," to which the Ambassador replied that the matter is not complicated if it is addressed in arbitration. Acosta repeated the government's position that Ecuadorian law governs the dispute and that ICSID does not have jurisdiction. When the Ambassador said that Ecuador should make its jurisdictional argument before the arbitral panel, Acosta said that would be a decision for the government's lawyer, the Solicitor General (Procurador General), to make. (Note: The acting Solicitor General told the Embassy in late January that he believes the GOE should defend its position before the arbitral panel, but was awaiting guidance from the Correa administration.)

#### Electrical Sector

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15. (C) Several times in the course of the meeting Acosta raised the problems of Ecuador's electrical sector (see also reftels b and c for a discussion of the problems). The basic problem, Acosta said, is that the sector is undercapitalized, the result of limiting the rates that electricity distributors can charge at levels below the cost of generating electricity. The other problem has been the government's failure to invest in the sector. He said that Ecuador has for long time understood its electricity problems (he asserted a 1984 analysis of the sector could still be used today), but has failed to act.

16. (C) Acosta said the best response to the tariff mismatch is to increase production of inexpensive electricity, hence his desire to address Machala Power's problem so it could expand its generating capacity. Acosta said that the government is already moving forward with a project to increase reservoir capacity on the same river as Ecuador's largest hydroelectric dam, Paute, which is currently underutilized. The project would be funded by the FEISEH petroleum reserve fund, which is financed by revenue from the former Oxy fields.

17. (C) Acosta criticized Guayaquil's electricity distribution company, CATEG, as very inefficient and corrupt. He said CATEG loses over 30% of the power that it distributes, compared to the Latin American standard of 10-12%. Acosta said that he is not looking to lay blame, but wants to find solutions to CATEG's problems. He contrasted CATEG's performance to that of distributors for Cuenca (8% loss) and Quito (11% loss).

#### Petroleum Sector

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18. (C) Moving to the oil sector, Acosta said that the current oil production contracts are unfair for the state, and would have to be renegotiated to establish a more equitable return for the state.

19. (C) Acosta volunteered that his ministry is working on regulations to allow for the sale of natural gas. Currently Ecuador's one natural gas field is managed by EDC, the sister company of Machala Power, and can only sell to Machala Power.

Acosta would like to create a framework so EDC (and hopefully eventually other producers) could sell to commercial customers. Acosta also said that Cuenca is interesting in building a natural gas pipeline to Cuenca from either the EDC field or a field in northern Peru, which would reduce its consumption of subsidized diesel and fuel oil.

¶10. (C) When asked about the status of Ecuador's proposed crude-for-refined-product swap with Venezuela (reftel a), Acosta said that the government is also looking at other options, since the cost of shipping crude and refined products between Ecuador and Venezuela is high. He said that the government is exploring refining options in Peru and Chile while Ecuador constructs a new refinery.

#### Fuel Subsidies

¶11. (C) Acosta acknowledged that the GOE heavily subsidizes refined petroleum products and that these subsidies "do not have a future" (note: the 2007 budget estimates fuel subsidies will total \$2.3 billion). He said that a significant portion of the refined products are smuggled out of the country. He had met with former Minister of Defense Larriwa shortly before she died to discuss how the military could help combat smuggling of refined products.

¶12. (C) The Ambassador asked whether the government is considering targeted subsidies instead of subsidizing all fuel. Acosta said that targeted subsidies are possible, but would be very complicated and the government would need to be very creative. He added that he is not opposed to all subsidies, and that some are good and some are bad.

#### Transparency

¶13. (SBU) Acosta said that he wants to bring transparency to Ecuador's petroleum and mining sector. He said that he had met with an NGO, Revenue Watch, both before and after he became minister, and he is planning to sign an agreement with the NGO. He noted other nations, including Peru, also have agreements with Revenue Watch.  
BITS  
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¶14. (C) As an aside to his discussion of the Oxy case, Acosta said that the bilateral investment treaty (BIT) with the United States is not reciprocal, since "parts" do not apply to Ecuadorian firms operating in the United States. (Comment: it was not clear what parts Acosta believes are not reciprocal.) He went on to say that BITS are not the solution to Ecuador's investment problems; Ecuador has signed 25 BITS, and investment has not increased as a result.

¶15. (C) Acosta said that investment will go where there are business opportunities. He noted that Colombia has only two BITS but attracts more investment than Ecuador. He continued that Ecuador needs to strengthen its legal framework to promote investment.

#### Bio Notes

¶16. (SBU) Acosta's family has long been associated with Ecuador's banking sector. His grandfather was manager of what is now Ecuador's largest bank, Banco de Pichincha, and his cousin is currently the bank's vice president. His father served as Superintendent of Banks. Acosta has stayed away from the banking sector, and lived 10 years in Germany, where he obtained a degree in Energy Economics at the University of Cologne. He also served as a vice-consul in the Ecuadorian Embassy in Bonn.

¶17. (SBU) Acosta told the Ambassador that he loves jazz, and that there is much that he could learn from the United States. He said he does not know the United States well, except for New York, where his son studied and now works for

a bank.

Comment

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¶18. (C) Acosta was open, frank, and friendly throughout the meeting. Before taking office, he was known for his left-leaning newspaper columns that were often critical of U.S. economic policies. In his meeting with the Ambassador, Acosta largely came across as a pragmatic would-be problem solver. His frank discussion of Ecuador's electric sector and acknowledgement of the valuable contribution that private investors can play in the electric and natural gas sectors was refreshing. However, a notable shortcoming of Acosta's problem-solving presentation is that in at least this meeting he danced around one big economic challenge ) reducing Ecuador's large subsidy bill ) and did not even mention another huge challenge ) falling oil production, largely due to Ecuador's highly corrupt and inefficient state oil company (septel).

¶19. (C) Acosta also has some strongly-held views, as seen in his criticism of oil production contracts, BITs, and the "neo-liberal/neo-mercantilistic" model. There will be tension between these views and Acosta's desire to be a problem-solver. How that tension plays out could determine whether U.S. energy investors make any progress with their investment disputes or Ecuador successfully addresses its energy sector challenges.  
JEWELL